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FOLLOWING TRUST FUNDS.—TRUST FUNDS MINGLED IN ONE DEPOSIT WITH FUNDS OF THE TRUSTEE.—When a trustee, or one standing in that relation to the property of another, wrongfully mingles trust funds with funds of his own in a bank deposit, and alternately checks thereon and makes fresh deposits, how far *should* equity go in enforcing the rights of the *cestui* against the *deposit?*

The vast majority of the courts, in attempting to work out the *cestui's* right, apply two theories, the first being the rule first laid down in *Knatchbull* v. *Hallett*,[1] that as between the trustee or his creditors and the *cestui que trust*, if the depositor subsequently draws out a portion of the mingled deposit, equity *presumes* that he intended to draw on his own funds rather than on those of the *cestui*. Under this theory, so long as his general balance in bank *does not fall below the amount of the trust fund*—even though numerous fresh deposits be made, and continuous checking occur—the trust fund is *presumed* to remain intact.[2] But, (and here is where it is believed this theory stops too short) if the trustee's

[1] L. R., 13 Ch. Div. 696 (1878).
[2] Nat. Bk. *v*. Ins. Co., 104 U. S. 54, 26 L. Ed. 693 (1881); Hall *v*. Otis, 77 Me. 122 (1885); *In re* A. O. Brown & Co., 189 Fed. 432 (1911).

general balance *ever falls below the amount of the trust fund,* to that extent the trust fund has been encroached upon and the *cestui's* lien can only attach to what is left. New deposits of the wrongdoer's own funds thereafter made, cannot revive the lien and extend it to the new deposits [3]—*unless there be proof that such new deposits were meant as a restoration of the depleted trust fund.*[4]

The second theory is that equity regards the mingled fund as charged with an equitable lien in favor of the *cestui* to the extent of his interest therein.[5] Under this theory the *cestui* may claim either what is left of the trust fund in the mingled account, or he may claim property purchased with the fund or part of it. It will therefore be seen that the rights of the *cestui* can sometimes be worked out much more completely under the lien theory than by an invariable application of the first rule. For example, let us suppose that a trustee mingles $100 of a trust fund with $100 of his own, and then draws out $100 with which he purchases property, and that subsequently he squanders the other $100. If it were presumed in this case that the trustee first drew on his own fund, then there would be no property to which equity could attach a trust in favor of the *cestui.* But in this case equity does not apply the function of the first theory, since it does not permit a

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[3] Schuyler *v.* Littlefield, 232 U. S. 707 (1914); Merc. Trust Co. *v.* St. Louis, etc., R. Co., 99 Fed. 485 (1900); Metropolitan Nat. Bk. of Kan. City *v.* Campbell Comm. Co., 77 Fed. 705 (1896); Cavin *v.* Gleason, 105 N Y. 256, 11 N. E. 504 (1887); *In re* Mulligan, 116 Fed. 715, 719 (1902). Excellent case supporting this view. Hewitt *v.* Hayes, 205 Mass. 356, 91 N. E. 332, 137 Am. St. Rep. 448 (1910). In the last case cited the rights of more than one *cestui* were involved, and the court, *as between the different cestuis*, applied the Rule in Clayton's Case, discussed *infra.* Other courts, notably the Federal Court in *In re* T. A. McIntire & Co., 181 Fed. 960, 104 C. C. A. 424 (1910), it is believed with better reason, apply the rule of *pari passu* and let the *cestuis* share ratably; Spokane County *v.* First Nat. Bk., 68 Fed. 979, 16 C. C. A. 81 (1895); Boone County Nat. Bk. *v.* Latimer, (C. C.), 67 Fed. 27 (1895).

[4] State Sav. Bk. *v.* Thompson, 88 Kan. 461, 128 Pac. 1120 (1913); Perkins *v.* Perkins, 134 Mass. 441 (1883); Supreme Lodge *v.* Liberty Trust Co., 215 Mass. 27, 102 N. E. 96 (1913).

[5] Englar *v.* Offutt, 70 Md. 78, 16 Atl. 497, 14 Am. St. Rep. 332 (1889); Standard Oil Co. *v.* Hawkins, 74 Fed. 395, 20 C. C. A. 468, 33 L. R. A. 739 (1896); Peak *v.* Ellicott, 30 Kan. 156, 1 Pac. 499, 46 Am. Rep. 90 (1883); Davenport Plow Co. *v.* Lamp, 80 Iowa 722, 45 N. W. 1049, 20 Am. St. Rep. 442 (1890). In Frelinghuysen *v.* Nugent, (C. C.), 36 Fed. 229, 239 (1888), it was said, "Formerly the equitable right of following misapplied money or other property into the hands of the parties receiving it, depended upon the ability of identifying it; the equity attaching only to the very property misapplied. This right was first extended to the proceeds of the property, namely to that which was procured in place of it by exchange, purchase, or sale. But if it became confused with other property of the same kind, so as not to be distinguishable, without any fault on the part of the possessor, the equity was lost. Finally, however, it has been held as the better doctrine that confusion does not destroy the equity entirely, but converts it into a charge upon the entire mass, giving the party injured by the unlawful diversion a priority of right over the other creditors of the possessor."

wrong to be worked by a legal presumption.[6] In all other cases, where it is in the interest of the *cestui* to do so, equity *conclusively presumes* that the trustee intended to draw from his own portion of the mingled funds, as long as he has any part therein, rather than from that of the *cestui*.

Now our quarrel is with the last part of this rule and our criticism is that it stops too short, short of complete justice and short of the necessary conclusion to which its own logic must inevitably carry it.

It *conclusively presumes* that the trustee intends to draw first on his own funds, but it does not presume that he intends to restore the *cestui's* funds when he makes later deposits. It can sufficiently *identify* the trust part of the mingled fund as long as the deposit never falls below the amount of the trust account, even though there be numerous withdrawals and fresh deposits. But if the deposit ever falls below the amount of the trust funds, it fails, and no new deposits thereafter can ever restore it. The reason given for this is that the trust *res* must be *traced* and *identified*. And yet if it can be proved that the deposits were made with the *intention of* restoring, this difficulty is not encountered. But how can the *intention* with which the fresh deposit was made affect the *identity* of the *res?* And if this *intention is necessary,* why can it not be *conclusively presumed* in this case as in the former? We ask further why this *conclusive presumption,* (often contrary to fact) is indulged in the first instance. We answer, FIRST, because the law presumes innocence rather than guilt, honesty rather than dishonesty,[7] and SECOND, to protect the interest of the *cestui* and prevent his property being taken for the payment of another's debt. We ask, finally, if both these ends would not be served in equal measure by a like presumption of intention in the case of *deposits* as in the case of *withdrawals*. If honesty requires that he do not *encroach* on the trust fund, does it not as well require that, having encroached, he *restore* as soon as possible? Will the law presume that he does not intend to act wrongfully, as long as this is possible, but after the wrong is done refuse to presume an intention to make amends?

And what of the *cestui's* interest? Should that be made to depend upon the mere intention of a faithless trustee? Of course where the rights of *bona fide* purchasers or creditors intervene and would be unduly prejudiced, the right of the *cestui* must, to that extent, yield, which is true in all cases, whether the *res* can be readily identified or not; but how are the rights of such third parties more prejudiced by presuming that the trustee has restored money wrongfully appropriated than by presuming that he used

[6] *In re* Oatway, 2 Ch. 356 (1903); Lamb *v.* Rooney, 72 Neb. 322, 100 N. W. 410, 117 Am. St. Rep. 795 (1904); Primeau *v.* Granfield, 184 Fed. 480 (1911); Brennan *v.* Tillinghast, 201 Fed. 609 (1913).

[7] Wilcox *v.* Wilcox, 46 Hun. (N. Y.) 32, 40 (1887); Grant *v.* Riley, 44 N. Y. S. 238, 15 App. Div. 190 (1897); U. S. *v.* Kenney, 90 Fed. 257 (1898).

his own money rather than that of the *cestui?* It is too clearly apparent that the two cases represent the same situation approached from opposite directions.

As said by one commentator on the subject:[8]

> "If, however, the claimant's money was deposited in a special trust account, and the wrongdoer withdraws a part and then deposits his own funds, it may well be held that *regardless of his intent;* the new deposit shall be treated as a restoration. Here the wrongdoer has put the money where it ought to be. He may be said to have performed to that extent his duty of reparation, *whether he intended to make restoration* or not." (Italics ours).

And for this statement he cites several cases.

And it was further said, in an able opinion by Mr. Justice Kellogg, in *United Nat. Bank, etc.* v. *Weatherby,*[9]

> "The claim is made by the administratrix that the several withdrawals and restorations made by Weatherby (trustee) in his lifetime operated to extinguish the *identity* of the money originally deposited belonging to these companies (the *cestuis que trustent*). The complete answer to that, it seems to me, is that such withdrawals were wrongful, whether intentional or inadvertent, and *presumptively* the wrongdoer by making subsequent deposits intended to make restoration and right the wrong. Under such circumstances, the *cestuis que trustent* have a right to adopt acts done for their benefit, and *as against all the world besides* the act of restoration is *conclusive* until at least it is shown that the money used to make restoration belonged to someone besides the wrongdoer. The act of restoration impressed the restored funds with the same trust which attached to the money originally deposited." (Italics and words in parenthesis ours.)

Boiled down to the final analysis, the question of the *identity* of the *res* should have little to do with this question except in those cases where it is an essential element of justice. All the courts do not admit it, even when that is the inescapable effect of their decisions, but the substantial rejection of *identity* as a test of the right to follow trust funds is apparent in a great majority of cases, and the distinctions made to keep a pretense of following it are often highly technical. The identity of funds in bank, for instance, exists only in the conception, and it is not discarded only because justice demands that the trust attach. And the courts still labor, in part, with the technicalities of the past, under rules laid down when equity was in its infancy.

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[8] 27 Harvard Law Review 125, 137 (1913). See also Gorman *v.* Littlefield, 229 U. S. 19 (1913).

[9] 70 App. Div. (N. Y.) 279, 75 N. Y. S. 3, 6 (1902). See also State Sav. Bk. *v.* Thompson, *supra*, note 4; Supreme Lodge *v.* Liberty Trust Co., *supra*, note 4.

We quote from an opinion of Church, Ch. J.: [10]

> "My agent collects $100 rent for me and puts the bills in one pocket and takes the same amount from another pocket and deposits it and notifies me. Are my rights gone by the change of money? I think not."

There is probably no one who would deny that a trust would attach to such a deposit, yet *identity* is plainly gone. The deposit is not even the *proceeds* of the original *res.*

Or we will draw an illustration of our own. Suppose a trustee deposits $100 trust funds in bank, and later he *mails* $100 of his own to the same deposit. Suppose still later he draws out $100 and that because of an inadvertence in the mails his withdrawal reaches the bank before his fresh deposit, thus wiping out the trust fund altogether before the new deposit arrives. Will anyone say that the *cestui's* rights against the *deposit* are all gone? But it may be answered, here was *proof of a proper intention.* Then reverse the case. The withdrawal is mailed first and the fresh deposit last, but by a like inadvertence of the mails the fresh deposit reaches the bank before the wrongful withdrawal. No one will deny that the trust fund remains intact, yet here was *proof of an improper intention.* Here we will doubtless be answered that regardless of intention the trust fund, by the rule laid down, remains intact and hence never loses its *identity.* And so it goes with the courts, striving after substantial justice, but bound by precedent, seeking to justify themselves first on the principle of identity, next on the *proof* of *intention,* when neither is essential. And we think it can be proved that neither is essential. On the question of identity we have already said much. On this point, therefore, we think it will be sufficient to add one more excerpt each from two opposing opinions, the first from *Mercantile Trust Co.* v. *St. L. & San Francisco Ry. Co.,*[11] in which the court says:

> "It was conceded at the argument that if . . . the whole account had been drawn out . . . so that nothing remained, the *tracing* or *identification* of the trust fund would no longer have been possible, and that no subsequent deposits would have been subject to the original trust. This concession was manifestly made on the ground that *no part of the original trust fund could be said to be mingled with that which was subsequently deposited.*" (Italics ours.)

For comment we refer again to our illustration of the fresh de-

[10] Van Alen *v.* Am. Nat. Bk., 52 N. Y. 1 (1873). See also Baker *v.* Bank, *supra*, note 4. "Conceding that W. & Bro. (insolvent trustees) used the specific proceeds for their own purposes, and their identity was lost, yet when they made up the amounts so used, and deposited them in the trust account, the amounts so deposited were impressed with the trust in favor of the principals and became substituted for the original proceeds and subject to the same equities."

[11] *Supra*, note 3.

posit delayed in the mails, and quote from the able opinion of Hand, District Judge, *In re A. O. Brown & Co.*:[12]

> "The question is whether we should not *assume* that the broker, in taking from other funds enough to buy an equal number of shares of stock, did not intend *pro tanto* to attribute that much of his own funds to making good his default. By way of analogy, suppose that an agent *depletes* a bank deposit made in his name as agent. Subsequent deposits in that fund would go to make good the former conversion, *and the general creditors could not complain.* . . . To adopt the analogy suggested by Mr. Justice Holmes in his opinion in *Richardson* v. *Shaw*,[13] suppose an elevator man has depleted the elevator below the amount due all depositors; when he subsequently puts back into the elevator enough, or part of enough, wheat to answer his obligations to all, the claimants become co-owners of it. Could the elevator man's general creditors claim that they were entitled to the subsequent accretions? Or suppose it could be shown that he had entirely emptied the grain elevator; is there any doubt that his subsequent filling of it, or partial filling of it, must be *assumed* to be an appropriation by him of so much of his property to make good his conversion? The analogy in law seems to me to be complete in spite of the diversity of the subject matter." (Italics ours.)

We will now dispose of the supposed necessity for *proof* of intention, and next we hope to show the true principles upon which the rights of the *cestui* should be founded.

We will lay it down as the first undeniable principle that the encroachment on the trust fund by the trustee is wrongful, and we will take as an extreme example the case where the wrongdoer *emphatically denies* that his subsequent deposits were made with the intention of restoring the trust funds. *Can he be allowed to make such a denial?* A thief who has stolen a horse and sold it at a good price is estopped, upon being sued in assumpsit for the price on a count of money had and received, to deny that he acted honestly. We quote again from the opinion of Jessel, M. R., in Knatchbull *v.* Hallett:[14]

> "Nothing can be better settled, either in our own law, or, I suppose, the law of all civilised countries, than this, that where a man does an act which may be rightfully performed, he cannot say that the act was intentionally and in fact done wrongly. . . . Wherever it can be done rightfully, he is not allowed to say, against the person entitled to the property or the right, that he has done it wrongfully."

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[12] 171 Fed. 254, 256 (1909).
[13] 209 U. S. 365, 385, 28 Sup. Ct. 512, 52 L. Ed. 835 (1908).
[14] *Supra.*

And Baggallay, L. J., in the same case, discussing the earlier case of *Pennell* v. *Deffell*,[15] said:

> "Had it been argued on the part of the Appellants that the payment of the £72 16s 3d Green (trustee) on the 5th of Oct. ought to be treated as a repayment *pro tanto* of the £107 improperly drawn out by him on the 4th, before any blended account existed, the contention could hardly have been deemed unreasonable; no such contention, however, appears to have been raised."

If, then, the wrongdoer cannot deny the presumption that his intention was to restore, who can? Clearly only such creditors as would be injured by such a presumption and only in those cases where the *cestui* himself is estopped to set it up. All the courts now hold that the intention of the wrongdoer is immaterial as to *withdrawals* made by him on the mingled deposit, and the distinction drawn as to his intention regarding *deposits* does not seem to be founded on reason.

The true principles involved, then, become at once apparent. They are the old and favorite maxims of equity and it is passing strange that they have never been invoked in this connection. We enumerate them:

1. "A man cannot, by abuse of trust, acquire money for distribution among his general creditors." [16]
2. "Equity will not allow the unjust enrichment of one man at the expense of another."
3. "Equity will not allow the property of one person to be taken for the debt of another."
4. "A creditor, in the absence of the element of estoppel, stands in the shoes of his debtor."
5. "Equity *imputes* an *intention* to *fulfill* an obligation."
6. "Equity looks to the substance rather than to the form."

These are sound principles of equity, universally accepted without question yet it seems every single one of them is violated by the rule under criticism. When a man puts trust funds in a bank and then draws them out and later replaces them, and his creditors are allowed to claim equally therein with the *cestui*, the first three of these maxims are violated. As against the trustee himself no one denies that the *cestui's* rights against the new fund are paramount. The same is true as against the trustee's estate. Conse-

[15] 4 DeG. M. & G. 372, 43 Eng. Reprint 551 (1853), overruled by Knatchbull *v.* Hallett, *supra.*

[16] First Nat. Bk. *v.* Hummel, 14 Col. 259, 272, 23 Pac. 986, 8 L. R. A. 788, 20 Am. St. Rep. 257 (1890). By Pattison, C, "Can a man, by an abuse of trust or violation of his fiduciary relations, acquire moneys for distribution among his general creditors at his decease? * * * the *estate* of no man can be increased by a wrong committed by him." "An abuse of trust can confer no rights on the party abusing it, or on those who claim in privity with him." 2 STORY, EQUITY JURISPRUDENCE, 10th ed., § 1258.

quently, (in the absence of estoppel) when the *cestui's* priority over the general creditors is taken away, the fourth maxim is violated. When a court of equity refuses to *presume* an intention by the trustee to restore misappropriated funds, it violates the fifth maxim; and when it demands, as a prerequisite of justice, that *identity* be *traceable* it violates the sixth.

Nor are we unprepared to follow our reasoning to its logical and extreme conclusion. We will be asked: if funds traced into a bank account are subject to the trust through all the fluctuations of the account, why would not the same be true of funds traced into the trustee's general estate? In truth we can see no difference in principle. Indeed, if the estate of the insolvent trustee is thereby swelled for the payment of his debts, such a conclusion is inescapable if the first three maxims quoted above are not to be violated. This was also the reasoning of the great James Barr Ames, from whom we quote:[17]

> "Let us now suppose that the misappropriated *res* cannot be traced into any specific land, chattels, bank deposit or into the money in a bank, but that the Court is convinced that the fund for distribution among the creditors of the wrongdoer is larger than it would have been but for the misappropriation. Should the victim of the misappropriation come in ahead of the general creditors? Obviously he cannot establish any trust or lien for want of any specific *res*. But in justice he should be treated as a preferred creditor *as to the excess of the actual fund for distribution above what it would have been if the misappropriation had not been made. The general creditors should not make a profit by their debtor's misuse of another's property and at the expense of the defrauded owner.*" (Italics ours.)

And there are numerous cases which sustain this view.[18]

This suggestion was made in *Cavin* v. *Gleason,*[19] but was rejected by the Court, which said:

> "We think this is quite *too vague an equity for judicial cognizance,* and we find no case justifying relief upon such a circumstance. In a very general sense all creditors of an insolvent may be supposed to have contributed to the assets which constitute the residuum of his estate." (Italics ours.)

[17] 19 Harvard Law Review, 511, 521 (1906).

[18] McLeod *v.* Evans, 66 Wis. 401, 28 N. W. 173, 57 Am. Rep. 287, 290 (1886); Standard Oil Co. *v.* Hawkins, *supra*, note 5; State *v.* Bruce, 17 Idaho, 1, 102 Pac. 831, 134 Am. St. Rep. 245, 249 (1909). This last is an excellent discussion with copious citations in point. Myers *v.* Board of Education, 51 Kan. 87, 32 Pac. 658, 37 Am. St. Rep. 263 (1893); Peak *v.* Ellicott, *supra*, note 5. See also, *In re* National Permanent Benefit Bldg. Soc., L. R. A., 5 Ch. App. 309 (1869); *In re* Wrexham, etc., R. Co. L. R., 1 Ch. 440 (1899); Blackburn Bldg. Soc. *v.* Cunliffe, L. R., 22 Ch. Div. 61 (1882); Slater *v.* Oriental Mills, 18 R. I. 352, 27 Atl. 443 (1893).

[19] *Supra*, note 3.

Forbearing any comment on judicial self-stultification, we will admit that the last sentence of this excerpt is strictly true, but the learned judge evidently failed to note the vast difference between the two cases, the vital distinction that the creditor contributed *voluntarily* and upon the *personal credit* of the debtor, while the *cestui's* property is taken without his consent and illegally and in breach of fiduciary relations, and applied to the payment of the debts of another. And this distinction is now appreciated by the courts of many progressive states. In *McLeod* v. *Evans,*[20] the court says:

> "We do not understand that it is necessary to trace the trust fund into some *specific property* in order to enforce the trust. If it can be traced into the *estate* of the defaulting agent or trustee, this is sufficient." (Italics ours.)

And the reasoning in *State* v. *Bruce,*[21] seems eminently sound to us:

> "We fail to see what difference it can make in point of fact, reason or law whether the money was used in buying bonds, mortgages and other paper to *add to the general assets* of the bank, or in *discharging the debts* of the bank (and thus decreasing its liabilities). In either event, it adds to or appreciates the body and *value* of the bank's assets. If the money is used today to pay the bank's debts and it suspends business tomorrow, the indebtedness of the bank tomorrow will be just that much less than it would otherwise have been as the amount paid out represents. The assets of the bank are worth more (to its creditors) when the bank's debts amount to only $500,000 than when they amount to $600,000." (Italics and words in parenthesis ours.)

The present state of the law seems to be a result of putting new wine into old bottles, of patching old clothes with new cloth. This is more apparent when we trace the steps by which equity has arrived at its present doctrine as to the tracing of trust funds.

In the earlier days, when equity was in its infancy, property, other than money, impressed with a trust, could be traced only as long as the identical *res* could be traced and identified. Later the *proceeds* of the original *res* could be so impressed, if not money, as long as it could be traced and identified, but *money* could in no case be followed because it had no ear-mark. Still later it was held in equity that money could be traced if the *identical coin* were kept separate, and so, upon the bankruptcy of the trustee it would not fall into his estate.

And in *Taylor* v. *Plumer,*[22] so great a chancellor as Lord El-

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[20] *Supra,* note 18.

[21] *Supra,* note 18.

[22] 3 M. & S. 562, 105 Eng. Reprint 721 (1815).

lenborough said that property the *proceeds of trust money* might be traced and identified, but that:

> "the means of ascertainment fail . . . when the subject matter is *turned into money* and mixed and confounded in a general mass of the same description." (Italics ours.)

But he adds, and this is very significant,

> "The difficulty . . . is a difficulty of *fact*, and *not of law.*" (Italics ours.)

In other words, it was not the *right* that was doubtful, but the difficulty of *identification,* supposed at that early age of equity to be essential to its enforcement, that precluded justice.

The next step taken by equity was in *Pennell* v. *Deffell,*[23] in 1853, a step overcoming, in some measure, the "difficulty of fact," mentioned by Lord Ellenborough, to the extent of applying the *Rule in Clayton's Case*[24] to trust funds mingled in bank with other money belonging to the trustee. This rule was that checks drawn against a bank account would, in absence of directions, come out of the several deposits in the order in which they were deposited.

This might sometimes help the *cestui* and again would not, depending on whether his money was the first or last deposited; but it was the first step away from the old doctrine, laid down by Lord Ellenborough in *Taylor* v. *Plumer, supra,* that money could not be followed into a mingled fund but that the *identical coins* must be identified.

Finally, the more sensible rule of *Knatchbull* v. *Hallett, supra,* was laid down in England in 1878, overruling the *Rule in Clayton's Case, supra,* as applicable to mingled trust funds, and establishing the *presumption* that when a trustee drew on mingled funds he intended to draw his own money until that was all exhausted. This was as far as justice required the court to go in this case, and it is as far as the majority of the courts have since gone, but a *dictum* of Lord Justice Baggallay, quoted above, in the same case, would seem to indicate that he would have carried it much further had it been necessary to complete justice. A few courts in this country have carried the principle to its logical conclusion, as indicated herein, but the majority have been content to rest where the law was carried by *Knatchbull* v. *Hallett.*

When it is remembered how technical our law is, how subservient to precedent,—when it is further remembered that *Pennell* v. *Deffell* was only decided in 1853 and *Knatchbull* v. *Hallett* only in 1878, it is not so surprising that a majority of our own courts have not yet gone the whole distance. As late as 1882 the Supreme Court of Maine held, in *Steamboat Co.* v. *Locke,*[25] that trust money could not even be traced into a mingled deposit. This

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[23] *Supra.*
[24] 1 Mer. 572, 35 Eng. Reprint 781 (1816).
[25] 73 Me. 370 (1882).

obliquity was corrected, however, in *Hall* v. *Otis*,[26] in 1885, in which case the rule of *Knatchbull* v. *Hallett* was applied.

Nevertheless, the principles contended for herein are supported by a very respectable minority and by reasons that appear to us unanswerable. It is evident, too, that many of the courts are growing restive under the inadequate test that precedent has laid down for them. Accordingly, it is confidently hoped that, having now rested, equity will soon take this next stride forward toward ultimate perfection.

H. L. W.

WHAT IS A DISCOUNTING?—If Smith is the holder of a negotiable note for $1,000.00, due in one year, he may go into the First National Bank, indorse the note, and transfer it to the cashier, who would give him the face value less 6% for the time that the note had to run, or $940.00. Now this Smith would tell the first friend he encountered that he had "discounted" the note. And the judge of the appellate court would, upon seeing these facts on the record, likewise pronounce this to have been a discounting of the note. But suppose that Smith had not indorsed the note. Would that alter the nature of the transaction? Or suppose that instead of getting $940.00 for the note, Smith had asked the cashier, "What will you give me for it?" The cashier after looking at the name on the paper would probably offer Smith $900.00. Smith would then indorse the note and hand it to the cashier. What is that transaction? Is that a discounting?

In the first example of the transfer of the note, which was agreed to be a discounting, there where two elements: (a) an indorsement, and (b) a price arrived at by figuring so much percent off the face value of the note for the time that it had to run. Must both of these elements be present to constitute the transfer a discounting, or only one?

Let us first look at the method of determining the price. Is this counting off of a certain percentage a necessary element of a discounting? The ordinary man would, I think, say that it is. Discount is defined as a deduction made for interest, in advancing money upon, or purchasing, a bill or note not due; payment in advance of interest upon money.[1] Common sense would say that the verb "to discount" would mean nothing more than a transfer or a sale at a discount. The idea of an advance in the nature of interest is, in the lay mind, inseparably connected with a discounting. And this argument from the common acceptance of the English language is in accord with the decisions reached in the adjudicated cases.[2]

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[26] *Supra*, note 2.

[1] WEBSTER'S NEW INTERNATIONAL DICTIONARY (1920).

[2] Fleckner *v.* Bank of U. S., 8 Wheat. 338, 5 L. Ed. 631 (1823); Bank *v.* Johnson, 104 U. S. 271, 26 L. Ed. 742 (1881); Danforth *v.* Bank, 48 Fed. 271, 1 C. C. A. 62, 17 L. R. A. 622 (1891); Morris *v.* Third National